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No. [illegible]

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October Term, 1940

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# INDEX



## CITATIONS

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# In the Supreme Court of the United States

OCTOBER TERM, 1940

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No. 36

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

*v.*

WALTER C. JANNEY AND PAULINE F. M. JANNEY

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*ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT*

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**BRIEF FOR THE PETITIONER**

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**OPINIONS BELOW**

The opinion of the Board of Tax Appeals (R. 23–27) is reported in 39 B. T. A. 240. The opinion of the Circuit Court of Appeals (R. 32–36) is reported in 108 F. (2d) 564.

**JURISDICTION**

The judgment of the Circuit Court of Appeals was entered December 26, 1939 (R. 36–37).[1] The petition for a writ of certiorari was filed March 26,

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[1] The date of the judgment is erroneously given in one place (R. 37) as December 26, 1940.

1940, and was granted April 29, 1940 (R. 37). The jurisdiction of this Court rests upon Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

## QUESTION PRESENTED

Whether, under the Revenue Act of 1934, the filing of a joint return permits the husband's capital losses to be deducted from his wife's capital gains.

## STATUTE AND REGULATIONS INVOLVED

The pertinent provisions of the Revenue Act of 1934 and of the regulations promulgated thereunder will be found in the Appendix, *infra*, pp. 34–37.

## STATEMENT

The stipulation of facts (R. 8–22), adopted by the Board of Tax Appeals as its findings (R. 24) may be summarized as follows:

The respondents are husband and wife and reside at Bryn Mawr, Pennsylvania (R. 8). During 1934 the wife, Pauline F. M. Janney, realized net gains from the sale of capital assets in the sum of $126,303.52. The amount of such gains to be taken into account under Section 117 (a) of the Revenue Act of 1934 (set out in the Appendix) was $94,491. During 1934 the husband, Walter C. Janney, realized net losses from the sale of capital asests in the sum of $220,687.06, of which the amount to be taken into account under Section

117 (a) of the Revenue Act of 1934 was $91,963.35 (R. 8–9).[2]

The respondents filed a single joint income tax return for the year 1934 (R. 8). In this return they reported a capital gain of $2,527.65, which represented the difference between the wife's adjusted capital gains ($94,491) and the husband's adjusted capital losses ($91,963.35) (R. 9–10, 13).

In auditing the return the Commissioner held, in accordance with Article 117–5 of Regulations 86, that the losses sustained by the husband could not be applied to reduce the gains realized by the wife and that the husband's losses accordingly could be deducted only to the extent of his own gains plus $2,000 (R. 10). By reason of this holding the Commissioner increased the capital gain reported by respondents by $89,963.35 (R. 10). On the basis of this adjustment, and of another adjustment not here involved, the Commissioner determined a deficiency of $37,109.29 (R. 5–6).

The Board of Tax Appeals sustained the Commissioner's decision on the capital loss issue and

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[2] The sum of $126,303.52 represents Mrs. Janney's capital gains less her own capital losses (R. 9). The sum of $220,-687.06 represents Mr. Janney's capital losses less his own capital gains (R. 9). The item of $94,491 stated to represent the percentage of Mrs. Janney's capital gains which may be taken into account and the item of $91,963.35 stated to represent the percentage of Mr. Janney's losses to be taken into account are based on these net gains and net losses.

determined a deficiency of $36,700.60 (R. 27). The Circuit Court of Appeals reversed the Board (R. 37). This Court granted certiorari (R. 37).

### SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that Section 117 (d) of the Revenue Act of 1934, either alone or in conjunction with Section 51 (b) (2), permits losses sustained by one spouse on the sale of capital assets to be applied against the gains of the other spouse from similar sales, if a joint return is filed.

2. In not holding that under Section 117 (d) and Section 51 (b) (2) a loss sustained on the sale of capital assets by one spouse is deductible only to the extent of his or her gains from similar sales (plus $2,000), even though a joint return is filed.

3. In not holding that the deductions which may be entered in a joint return are those to which each spouse, separately considered, is entitled.

4. In not holding that regulations promulgated under Section 51 (b) (2) and Section 117 (d) of the Revenue Act of 1934 were valid regulations which controlled the disposition of this case.

5. In holding that Article 117-5 of Regulations 86 is inconsistent with Section 51 (b) (2) of the Revenue Act of 1934 and is invalid.

### SUMMARY OF ARGUMENT

Sections 23 (j) and 117 (d) of the Revenue Act of 1934 together provide that losses from the sale

of capital assets shall be allowed as deductions only to the extent of $2,000 plus gains from such sales. Section 51 (b) permits a husband and wife to make a single joint return, in which case the tax shall be computed on the aggregate income.

It is the Government's position that even if a joint return is made the husband's capital losses can be deducted only to the extent of his own capital gains, and that gains of the wife cannot augment the deduction for the husband's losses. Deductions in a joint return may not be computed as if the husband and wife were one person. Whatever doubt might attend this question if the statute stood alone is eliminated, we submit, by the administrative construction, which has been impliedly approved by Congress.

1. With the exception of the decision below, the Government's position has been uniformly sustained by the courts. *Pierce* v. *Commissioner,* 100 F. (2d) 397 (C. C. A. 2d); *Demuth* v. *Commissioner,* 100 F. (2d) 1012 (C. C. A. 2d), certiorari denied, 307 U. S. 627; *Sweet* v. *Commissioner,* 102 F. (2d) 103 (C. C. A. 1st), certiorari denied, 307 U. S. 627; *Nelson* v. *Commissioner,* 104 F. (2d) 521 (C. C. A. 4th); *Gaines* v. *Helvering,* 111 F. (2d) 144 (C. C. A. 2d), pending on petition for certiorari, No. 113, this Term. And compare *Taft* v. *Helvering,* 111 F. (2d) 145 (C. C. A.

2d), pending on petition for certiorari, No. 183, this Term.

2. The provision in Section 51 (b) that if a joint return is made the tax shall be computed on the aggregate income contemplates that a husband and wife may, in such a return, utilize all deductions which would be allowable to either separately, including deductions of one spouse in excess of that spouse's gross income. But it carries no inference that if a joint return is made these deductions are to be determined as if the husband and wife were one person. Deductions are to be computed as in any other case, and the aggregate net income is then to be ascertained by combining the separate items of income and the separate deductions of each spouse.

Statutory limitations upon the allowance of a deduction which are contingent upon the amount or kinds of income of the taxpayer should not be abridged by treating husband and wife as a single taxpayer if they elect to file a joint return. There is no general principle that husband and wife are to be treated as a single taxpayer for purposes of deductions if they file a joint return. Instead the cases have regarded them as separate taxpayers in computing deductions, except as Congress has specifically provided otherwise. *Van Vleck* v. *Commissioner,* 80 F. (2d) 217 (C. C. A. 2d), certiorari denied, 298 U. S. 656; *Commissioner* v. *Thomas,* 84 F. (2d) 562 (C. C. A. 5th);

*Commissioner* v. *Brumder,* 82 F. (2d) 944 (C. C. A. 7th).

3. Whatever doubt might attend the meaning of the Act if it stood alone it resolved by the administrative construction which has been tacitly approved by Congress. Ever since 1921 the Treasury has taken the general position that even in a joint return only those deductions can be taken "to which either spouse is entitled." Article 401 of Regulations 62. Under Section 23 (r) (1) of the 1932 Act, the predecessor of Section 117 (d) of the 1934 Act, the Bureau of Internal Revenue ruled that securities losses sustained by the wife might not be offset against securities gains of the husband, even though a joint return was filed. G. C. M. 15438, Cum. Bull, XIV–2, p. 156. And Article 117–5 of Regulations 86, promulgated under the Revenue Act of 1934 and explicatory of Section 117 (d) of that Act, explicitly provides that the limitation "on the allowance of losses of one spouse from sales or exchanges of capital assets is in all cases to be computed without regard to gains and losses of the other spouse upon sales or exchanges of capital assets." *This regulation unequivocally covers the question here at issue.* The interpretation given Section 117 (d) of the 1934 Act by this regulation received tacit Congressional approval through the enactment of identical statutory provisions in the Revenue Act of 1936 and of analogous provisions in the Revenue Acts of 1938 and 1939.

## ARGUMENT

### The Filing of a Joint Return Does Not, Under the Revenue Act of 1934, Permit the Husband's Capital Losses to be Deducted From His Wife's Capital Gains

Section 23 (j) of the Revenue Act of 1934 provides that losses from sales or exchanges of capital assets shall be allowed as deductions only to the extent provided in Section 117 (d). Section 117 (d) provides: "Losses from sales or exchanges of capital assets shall be allowed only to the extent of $2,000 plus the gains from such sales or exchanges." Section 51 (b) of the Act permits a husband and wife to make a single joint return "in which case the tax shall be computed on the aggregate income."

The two respondents in the present case are husband and wife and they filed a joint return for 1934. During that year the husband realized net losses of $220,687.06 from the sale of capital assets, of which $91,963.35 was to be taken into account in computing net income under Section 117 (a) of the Revenue Act of 1934.[3] During the same

[3] Section 117 (a) of the Revenue Act of 1934 (set out in the Appendix) provides that in the case of a taxpayer other than a corporation only certain enumerated percentages of the gain or loss recognized upon the sale or exchange of capital assets shall be taken into account in computing net income, the percentages being graduated downward according to the length of time for which the capital assets have been held.

period the wife realized net gains of $126,303.52 from the sale of capital assets, of which $94,491 was to be taken into account under Section 117 (a).

The court below held that the husband's net losses from the sale of capital assets might be deducted in the joint return to the extent of the wife's net gains from similar sales. It said that the provision of Section 51 (b) that if a joint return is used the "tax shall be computed on the aggregate income" necessarily means "that in arriving at joint net income both gross income and deductions of the spouses must be aggregated and treated as the income and deductions of a single taxpayer." (R. 34).

It is the Government's position that the husband's capital losses could be deducted only to the extent of his own capital gains plus $2,000, and that the gains of the wife could not be used to augment the permissible deduction for the husband's losses. It is, of course, admitted that if the spouses had made separate returns each could deduct his or her capital losses only to the extent of his or her capital gains. And we think that nothing in the statutory provision permitting a joint return implies that deductions are to be computed in such a return as if the husband and wife were one person. On the contrary, we think that deductions are to be determined separately for each spouse, and that their aggregate net income is then to be ascertained by combining their separate items of income and their separate deductions.

If, however, the statute is ambiguous, that ambiguity is resolved by the administrative construction, tacitly approved by Congress, in favor of the interpretation which we here urge. Article 117-5 of Regulations 86, promulgated under the Revenue Act of 1934, explicitly and admittedly covers the present case. This regulation was presumptively valid when issued. It has since been approved by Congress, by its reenactment in the Revenue Act of 1936 of statutory provisions identical with those of the 1934 Act on which the regulation was based, and by its enactment of analagous provisions in the Revenue Acts of 1938 and 1939.

1. *The Decisions.*—With the single exception of the decision below in the present case, the position here taken by the Government has been uniformly upheld by the lower courts.[4] Substantially the same question which is here presented was resolved in favor of the Government in *Pierce* v. Commissioner, 100 F. (2d) 397 (C. C. A. 2d) That case has since been followed in *Demuth* v. *Commissioner,* 100 F. (2d) 1012 (C. C. A. 2d), certiorari denied, 307 U. S. 627; *Sweet* v. *Commissioner,* 102 F. (2d) 103 (C. C. A. 1st), certiorari denied, 307 U. S. 627; *Nelson* v. *Commissioner,* 104 F. (2d) 521 (C. C. A. 4th); and *Gaines* v. *Helvering,* 111 F.

[4] The decision below is commented upon and criticized adversely in (1940) 49 Yale L. J. 1279, and in (1940) 53 Harv. L. Rev. 681.

(2d) 144 (C. C. A. 2d), pending on petition for certiorari, No. 113, this Term. The *Gaines* case, like the case at bar, was decided under the Revenue Act of 1934. The other cases involved the cognate provisions of the Revenue Act of 1932. Section 23 (r) (1) of that Act provided that losses from sales or exchanges of stocks and bonds which were not capital assets should be allowed only to the extent of gains from such sales or exchanges, and Section 101 (c) (8) defined "capital assets" as property held by the taxpayer for more than two years. In each of those cases the courts held that the losses of one spouse from the sale of non-capital assets could not be deducted from the gains of the other spouse from similar sales, even though a joint return was used. The court below recognized that these cases support the Government's position, but declined to follow them (R. 33).[5]

Since the decision below, the Circuit Court of Appeals for the Second Circuit has held *per curiam,* upon the authority of its decision in the *Pierce* case, that the limitation on the deduction for charities to 15 percent of the taxpayer's net income (Section 23 (o) of the Revenue Act of 1934)

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[5] The Board of Tax Appeals also has consistently upheld the Government's position. *Pierce* v. *Commissioner*, 37 B. T. A. 225; *Montgomery* v. *Commissioner*, 37 B. T. A. 232; *Sweet* v. *Commissioner*, decided June 30, 1938, memorandum opinion, unreported; *Demuth* v. *Commissioner*, decided February 7, 1938, memorandum opinion, unreported.

must be computed with reference to the husband's and wife's separate net incomes, and may not, even though a joint return is filed, be computed on their combined net income. *Taft* v. *Helvering,* 111 F. (2d) 145, pending on petition for certiorari, No. 183, this Term.

2. *Meaning of the Act.*—The decision below in the present case relies largely upon the reasoning of Judge Learned Hand's dissent in the *Pierce* case. Both the opinion below and that of Judge Hand rest their rejection of the Government's position, not on any construction of Section 117 (d) in the present case or of Section 23 (r) (1) of the 1932 Act in the *Pierce* case, but on their interpretation of Section 51 (b). In his dissent in the *Pierce* case Judge Hand asserted that the privilege given by Section 51 (b) of filing a joint return was based upon disregarding the source of the deductions and of the items of income. 100 F. (2d) at 398, 399. The court below approved this reasoning, and similarly concluded that the provision that if a joint return is made the tax shall be computed on the aggregate income necessarily means that both gross income and deductions of the spouses be "treated as the income and deductions of a single taxpayer." (R. 341.)

This argument fails, we think, to distinguish between the undisputed proposition that the allowable deductions of both spouses are to be con-

solidated in a joint return, and the further proposition, here at issue, that the two spouses are to be regarded as a single taxpayer or as one person in determining what deductions are allowable in such a return. It overlooks, in other words, the fundamental distinction between "pooling" the deductions and items of income of the two spouses in a joint return and treating the two spouses as one person for the purpose of ascertaining what items of income and what deductions are to be entered in that return. If the capital losses of Mr. Janney in 1934 had been deductible in full, without limitation, those losses could have been pooled in the joint return with any other deductions allowable to Mr. Janney or to his wife, and their aggregate sum could have been deducted from the aggregate income of the two in determining their taxable net income. But Mr. Janney's capital losses were not deductible in full, without limitation. By Section 117 (d) the deduction was specifically limited to $2,000 plus capital gains. Section 51 (b) provides that if a joint return is filed the tax shall be computed on the aggregate income. But nothing in this provision suggests that the making of a joint return expands the measure of the deduction under Section 117 (d) to embrace the capital gains of both spouses.

The provision of Section 51 (b) in question has to do with the computation of the tax on the joint

return and not with determining what items of income should be reported, or what deductions are allowable, or the amount of permissible deductions. It unquestionably contemplates that a husband and wife may, in a joint return, use all deductions which would be allowable to either separately, including deductions of one spouse in excess of that spouse's gross income.[6] But it carries no inference that because a joint return is employed these deductions are to be determined as if the husband and wife were one person. On the contrary, it is most unlikely that Congress intended by Section 51 (b) to provide for different limitations

[6] The provisions of Section 51 (b) of the Revenue Act of 1934 were first enacted in that form in Section 223 of the Revenue Act of 1921, and were contained also in the various intervening revenue acts. The Revenue Act of 1918, Section 223, provided for the filing of joint returns but did not specify how the tax was to be computed if a joint return was filed. In Sol. Op. 90, Cum. Bull. No. 4, p. 236 (1921), the Solicitor of Internal Revenue ruled that under the 1918 Act the tax of a husband and wife filing a joint return was to be computed on their net aggregate income, and that the deductions of one spouse, if they exceeded his or her income, could be deducted from the gross income of the other. Apparently, however, some doubt existed as to right of taxpayers having income subject to surtaxes to file joint returns and have their tax computed in this fashion, and it was to resolve this doubt that there was inserted in the 1921 Act the provision that in joint returns the tax should be computed on the aggregate income. See S. Rep. No. 275, 67th Cong., 1st Sess., p. 17; H. Rep. No. 350, 67th Cong., 1st Sess., p. 13; Hearings before the Senate Committee on Finance on H. R. 8245, 67th Cong., 1st Sess., p. 74.

on the allowance of deductions depending upon whether joint or several returns were made. Rather the implication is that deductions are to be determined as in any other case and that the aggregate net income is then to be ascertained by combining the separate items of income and the separate deductions of each spouse. In other words, two calculations are required for determining the tax. The first is the calculation, which would be necessary in any return, of the separate items of income and the separate deductions. Section 51 (b) has no reference to this first calculation. It merely provides that after this calculation has been made, the items of income and the deductions of the husband and those of the wife are to be combined and the tax calculated on the aggregate net income thus determined. There is nothing in the phrase "aggregate income" to suggest that a husband and wife are to be considered as one person in determining what deductions are allowable, and it has never before been construed as prescribing such a rule, either by the courts, by the Board of Tax Appeals, or by the Treasury Department regulations.

Statutory limitations upon deductions which are contingent upon the amount or kinds of income of the taxpayer should not be curtailed by permitting husband and wife to elect to be treated as a single taxpayer by filing a joint return. There can be no question that such a con-

struction of the revenue act would in considerable part defeat such limitations upon deductions. For example, the statutory limitation here involved, Section 117 (d), provides that capital losses shall be offset only against capital gains, except that capital losses are deductible unconditionally up to $2,000. The operation of this limitation would be substantially curtailed if capital losses could be offset against capital gains of either spouse, since the two would be likelier to have capital gains than the spouse who suffered the losses would be alone. Again, the statutory provision involved in the *Taft* case, Section 23 (o), limits deductions for charitable contributions to 15 percent of the taxpayer's net income. This limitation, too, would be relaxed if a husband and wife making a joint return were treated as a single taxpayer, since the combined net income of husband and wife would normally exceed the individual income of the spouse making the contributions. Situations can be conceived with respect to both of these statutory limitations on deductions in which the single taxpayer theory urged by the Government would be advantageous to the taxpayer, and the contentions urged by respondents disadvantageous.[7] But, on

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[7] Section 117 (d) allows a deduction of $2,000 of capital loss from ordinary income, which would in some situations render advantageous to taxpayers the interpretation here urged by the Government. Thus, if both husband and wife had large capital losses and no capital gains, they could, under the separate taxpayer theory which we urge, each

the whole, the construction here urged by the Government is that calculated to give full effect to such statutory limitations on deductions and thus to produce maximum revenue. See (1940) 49 Yale L. J. 1279, 1284.

In the court below respondents argued, in effect, that to allow capital losses of one spouse to be offset against capital gains of the other spouse would not be inconsistent with the purpose of Section 117 (d). Specifically they pointed out that the legislative history both of Section 117 (d) of the 1934 Act and of its predecessor, Section 23 (r) (1) of the 1932 Act, shows that the purpose of Congress was to prevent taxpayers from escaping taxation on their ordinary incomes, that is on income from salaries, rents, dividends, etc., by utilization of deductions for security losses. See S. Rep. No. 665, 72d Cong., 1st Sess., p. 17; H. Rep. No. 704, p. 10, 73d Cong., 2d Sess., p. 10. And respondents argued that since to permit security losses of one spouse to be offset against security gains of the other spouse would

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take a $2,000 deduction, while under the theory of respondents but one $2,000 deduction would be allowable for both if a joint return were filed. See (1940) 49 Yale L. J. 1279, 1282. The spouses would still, however, have the option of filing separate returns.

Similarly, in the case of the limitation of charitable deductions to 15 percent of net income, the construction urged by respondents would be advantageous to the Government if one of the two spouses had no net income, *i. e.*, had deductions in excess of gross income. But there, too, the taxpayers would still have the option of filing separate returns.

not enable them to escape taxation on their ordinary incomes, Congress cannot have intended to prohibit such offsets.

This argument, carried to its logical conclusion, would permit capital losses sustained by one spouse to be offset against capital gains of the other spouse regardless of whether separate or joint returns were made. Moreover, while the basic purpose of Congress was doubtless to prevent security losses from being applied against ordinary income (except up to $2,000), Congress did not relieve capital gains from taxation, except as capital losses were available under the statute to offset them. And the normal reach of the tax on capital gains would be curtailed if husband and wife, by filing a joint return, could offset the capital losses of both against the capital gains of either.

There is no general principle that husband and wife are to be treated as a single taxpayer for purposes of deductions if they elect to file a joint return. "Even if they file joint returns, husband and wife apparently do not blend into a single taxpayer, at least for the purpose of the deduction provisions." Paul and Havens, *Husband and Wife under the Income Tax* (1936), 5 Brooklyn L. Rev. 241, 257.

Thus net losses sustained by the husband in a year in which he filed a separate return may not be carried over and deducted from the income of the wife in a joint return for the following year. *Van*

*Vleck* v. *Commissioner,* 80 F. (2d) 217 (C. C. A. 2d), certiorari denied, 298 U. S. 656. The court said (80 F. (2d) at 218), "Although the petitioners filed a joint return in 1930, each of them remained a separate and distinct taxpayer." Compare *Woolford Realty Co.* v. *Rose,* 286 U. S. 319.

Similarly, it was formerly held that losses sustained by one spouse in a bona fide sale of securities to the other spouse could be deducted in a joint return. *Commissioner* v. *Thomas,* 84 F. (2d) 562 (C. C. A. 5th); *Joseph E. Uihlein,* 30 B. T. A. 399, affirmed *sub nom. Commissioner* v. *Brumder,* 82 F. (2d) 944 (C. C. A. 7th); *Hill* v. *United States,* 12 F. Supp. 798 (C. Cls.); *Frank B. Gummey,* 26 B. T. A. 894; I. T. 2824 XIII–2 Cum. Bull. 293, overruling I. T. 1997, III–1 Cum. Bull. 149. Section 24 (b) (1) of the Internal Revenue Code, derived from Section 24 (b) (1) of the Revenue Act of 1938, now prohibits deductions for losses resulting from sales between members of a family, but this provision was adopted merely to prevent tax evasion. See H. Rep. No. 704, 73d Cong., 2d Sess., p. 23; 1939–1 Cum. Bull. 554, 571; 78 Cong. Rec. 2662. See also (1940) 53 Harv. L. Rev. 681, 682. It prohibits the deductions in question without reference to whether separate or joint returns are filed; clear proof that it carries no general inference that husband and wife are to be treated as a single taxpayer if they make a joint return. See (1940) 49 Yale L. J. 1279, 1283.

Formerly, also, some courts refused to hold spouses jointly and severally liable for the tax even though they filed a joint return. *Cole* v. *Commissioner,* 81 F. (2d) 485, 487 (C. C. A. 9th); *Crowe* v. *Commissioner* 86 F. (2d) 796 (C. C. A. 7th). The doubt engendered by these decisions was eliminated by the insertion in Section 51 (b) of the 1938 Act of a provision explicitly making liability with respect to the tax joint and several. Here too, however, the reason for the change was merely administrative expediency and not any theory that husband and wife are one taxpayer. See H. Rep. No. 1860, 75th Cong., 3d Sess., pp. 29–30; (1940) 49 Yale L. J. 1279, 1284. And see *infra,* pp. 31–32.

Section 51 (b), we have sought to show, carries no inference that spouses filing a joint return are to be treated as a single taxpayer for the purpose of computing limitations on deductions. And since husband and wife are not required to make a joint return the privileges stemming from the option to do so should not be increased beyond the apparent intention of Congress. If, however, it is thought that the general congressional policy to favor the family unit, embodied in Section 51 (c) and in the larger personal exemption accorded married taxpayers, encompasses the issue at bar, that policy conflicts with the specific congressional intention, expressed in Section 117 (d), stringently

to limit deductions for capital losses. "* * * the policy of mitigating the tax burden of the family as an economic unit might be balanced against that of limiting deductions to those specifically allowed." (1940) 53 Harv. L. Rev. 681, 682. This statutory ambiguity, or conflict of policies, if there be such, is appropriate for solution by administrative construction. Below respondents asserted no more than that the relevant provisions of the Act are ambiguous, and, standing alone, are compatible with either the construction urged by respondents or that urged by the Government.

3. *The administrative construction.*—Article 51-1 of Regulations 86, promulgated under the Revenue Act of 1934, and explicatory of Section 51 of that Act, reads:

> If the income of each is included in a single joint return, the tax is computed on the aggregate income and all deductions and credits to which either is entitled shall be taken from such aggregate income.

This provision is ultimately derived from Article 401 of Regulations 62, promulgated under the Revenue Act of 1921 (Section 223), which has been preserved in substance in succeeding regulations.[8]

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[8] See Article 401 of Regulations 65 and 69, promulgated, respectively, under the Revenue Acts of 1924 and 1926 (Section 223 of those Acts); Article 381 of Regulations 74 and 77, promulgated, respectively, under the Revenue Acts of 1928 and 1932 (Section 51 of those Acts); Article 51-1 of

As has been stated, Section 117 (d) of the Revenue Act of 1934 was derived, with modifications not here material, from Section 23 (r) (1) of the Revenue Act of 1932: the revenue acts prior to 1932 had not contained any comparable provision limiting deductions for stock losses. No regulations explicatory of Section 23 (r) (1) were promulgated under the Revenue Act of 1932.

However, in a letter of December 29, 1932, to the Commerce Clearing House, Inc. (1933 C. C. H., Federal Tax Rewrite Service, par. 6037) the Commissioner stated that in a joint return the wife's gains from sales of securities might be offset by the husband's losses from such sales, since a "joint return is treated as if it was the return of a single individual." The view thus expressed by the Commissioner was never embodied in any sort of Treas-

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Regulations 86 and 94, promulgated, respectively, under the Revenue Acts of 1934 and 1936 (Section 51 of those Acts).

The provision in question was somewhat amplified in Article 51–1–(b) of Regulations 101, promulgated under the Revenue Act of 1938 (Section 51). It there reads: "A husband and wife, if living together at the close of the taxable year, may elect to make a joint return (see Section 51 (b)), that is, to include in a single return made by them jointly the income and deductions of each, even though one has no gross income. In such a case, the tax shall be computed on the aggregate income and all deductions and credits to which either is entitled shall be taken from such aggregate income." This expanded version is retained as quoted in Sec. 19.51–1 of Regulations 103, promulgated under the Internal Revenue Code (Section 51).

ury ruling and was not published by the Government.

In G. C. M. 15438, Cum. Bull. XIV–2, p. 156 (1935), on the other hand, the Bureau of Internal Revenue ruled that under the 1932 Act losses sustained by the wife through sales of securities might not be allowed as an offset against gains derived by the husband from like transactions, even though a joint return were filed. This ruling did not refer to the December 29, 1932, letter. Following *Frank B. Gummey,* 26 B. T. A. 894; acquiesence, XIII–2 Cum. Bull. 8, it took the view generally that a husband and wife filing a joint return remain separate taxpayers for the purpose of determining their right to deductions.

Article 117–5 of Treasury Regulations 86, promulgated under the Revenue Act of 1934 and explicatory of Section 117 (d) thereof, squarely and admittedly covers the question here at issue. It reads:

> In the application of section 117, a husband and wife, regardless of whether a joint return or separate returns are made, are considered to be separate taxpayers. Accordingly, the limitation under section 117 (d) on the allowance of losses of one spouse from sales or exchanges of capital assets is in all cases to be computed without regard to gains and losses of the other spouse upon sales or exchanges of capital assets.

The provisions of Section 117 (d) of the Revenue Act of 1934 were retained in the same form in Section 117 (d) of the Revenue Act of 1936, and the provisions of Article 117-5 of Regulations 86 were retained in substantially the same form in Article 117-5 of Regulations 94. In both the Revenue Act of 1938 (Section 117) and that of 1939 (Section 212) considerable changes were made in the treatment of capital gains and losses, but in both provisions comparable to those of Section 117 (d) of the Act of 1934 were retained.[9] And Article 117-5 of Regulations 101, promul-

[9] Section 117 (d) (1) of the 1938 Act provided that in the case of a corporation losses from sales or exchanges of capital assets should be allowed only to the extent of $2,000 plus the gains from such sales or exchanges. Section 117 (d) (2) of that Act provided that "In the case of a taxpayer other than a corporation, short-term capital losses shall be allowed only to the extent of short-term capital gains." Section 117 (a) defined short-term capital gains and losses as those resulting from the sale or exchange of a capital asset held for less than 18 months, and defined long-term capital gains and losses as those resulting from the sale or exchange of a capital asset held for more than 18 months.

Section 117 of the 1938 Act was carried over into the Internal Revenue Code, but was thereafter amended by Section 212 of the Revenue Act of 1939 to eliminate the distinction between corporate and other taxpayers. As thus amended the Code provides (Sec. 117 (d)) that "Long-term capital losses shall be allowed, but short-term capital losses shall be allowed only to the extent of short-term capital gains."

gated under the Revenue Act of 1938, and Section 19.117-5 of Regulations 103, promulgated under the Internal Revenue Code, are each to the same effect as Article 117-5 of Regulations 86.[10]

The interpretation of the Act here urged by the Government is thus supported, in the first place, by the provision of Article 51-1 of Regulations 86, and its predecessors, that if a joint return is filed the tax is computed on the aggregate income and all deductions "to which either is entitled shall be taken from such aggregate income." This regulation clearly means that before any deduction may be entered in the joint return it must be a deduction to which either the husband or the wife, separately considered, is entitled under the law. As applied to the case at bar, it means that the husband's own right to deduct a loss on the sale of

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[10] Article 117-5 of Regulations 101 reads:

"ART. 117-5. Application of section 117 in the case of husband and wife.—(a) *Short-term capital gains and losses.*—Under the general rule with respect to taking deductions in a joint return of husband and wife (see article 51-1), a deduction which is not allowable in computing the net income of one spouse making a separate return is not allowable in a joint return made by both spouses. Hence, the limitation under section 117 (d) (2), relating to the allowance of short-term capital losses, is, in the case of one spouse, to be computed without regard to the short-term capital gains and losses of the other spouse, regardless of whether a joint return or separate returns are filed."

Section 19.117-5 of Regulations 103 follows Article 117-5 of Regulations 101 without substantial change.

capital assets must be established before the deduction may be entered in the joint return. Under Section 117 (d) of the 1934 Act the husband may deduct his losses from such sales only to the extent of gains from similar sales, plus $2,000. And under Article 51-1 no further deduction can be calculated and allowed in the joint return on the basis of the wife's gains.

That is the view which was taken of the regulation by the Circuit Court of Appeals for the Second Circuit in the *Pierce* case, decided under the 1932 Act. It said (100 F. (2d) at 398):

> * * * petitioners contend that when husband and wife file a joint return they become a taxable unit with the result that a loss of this character sustained by one spouse is an allowable deduction against gains of the same character received by the other. This contention cannot be sustained in view of the Treasury Regulations and judicial decisions in analogous cases. As already noted, the Regulations provide that the deductions to be taken from the aggregate income of husband and wife shall be those "to which either is entitled." Here neither was entitled to the deduction in question. * * *

As has been stated, Judge Learned Hand dissented in the *Pierce* case, and the reasoning of his dissent was approved in the case at bar (R. 34). Before reaching the conclusion, already discussed,

that the privilege of filing a joint return necessarily involves disregarding the source of deductions, Judge Hand put aside Article 381 of Regulations 77 (the predecessor of Article 51-1 of Regulations 86), as ambiguous. This conclusion he reached by finding uncertainty in the word "entitled". He said (100 F. (2d) at 398):

> The regulations—which I accept as law—add to these words [of Section 51 (b)] that "deductions * * * to which either spouse is entitled shall be taken from the aggregate income". To find the deductions to which "either spouse" is "entitled", one must look to those allowed individuals; in the case at bar to section 23, 26 U. S. C. A. § 23. Subdivision (e) of that section allows losses like those before us to be deducted, "subject to the limitations of subdivision (r)." The Commissioner argues that that clause imposes a condition upon the privilege, as opposed to a limitation upon its amount, so that in order to learn whether a spouse is "entitled" to any deduction whatever, it is first necessary to find out whether the limitation would extinguish it if he or she filed a separate return. The taxpayer answers that § 23 (e) grants the privilege, and therefore "entitles" the spouse to a deduction, and that subdivision (r) merely limits its amount when the joint net income is being computed. As a mere matter of words I can see nothing to prefer in either

> construction; it begs the question to say that the extent of the deduction under a separate return must be taken as a condition upon its existence. * * *

This reading of ambiguity into the regulation is, we submit, unwarranted: the alternative construction accepted by Judge Hand as plausible is hypertechnical and departs from the ordinary meaning of the word "entitled." Mrs. Pierce could not individually deduct her securities losses because under Section 23 (r) they could be offset only against securities gains, and she had none. Thus she was not, under any usual meaning of the term, "entitled" to a deduction for securities losses. It is artificial to suggest, as does Judge Hand, that perhaps she was "entitled" to the deduction and that the deduction was merely limited as to amount—limited, in the *Pierce* case, to zero—by her lack of securities gains. A deduction which cannot be taken is not, in any usual sense, a deduction to which a taxpayer is "entitled."

The court below apparently accepted Judge Hand's treatment of Article 51-1 (or, rather, of its predecessor); in addition it relied upon the Commissioner's letter of December 29, 1932, as showing an administrative construction, up to the promulgation of Article 117-5 of Regulations 86, contrary to the position now taken by the Government. See R. 33-35. This letter was an informal opinion,

never published by the Bureau of Internal Revenue as a ruling, and is not entitled to the weight given to Treasury Regulations (*Helvering* v. *N. Y. Trust Co.*, 292 U. S. 455, 468) or to published rulings of the Internal Revenue Bureau (see *Estate of Sanford* v. *Commissioner*, 308 U. S. 39, 52–53). Moreover, the only published ruling of the Bureau construing Section 23 (r) (1) of the 1932 Act is G. C. M. 15438, XIV–2 Cum. Bull. 156 (1935), and it is directly contrary to the letter. G. C. M. 15438 was not issued until after the Revenue Act of 1934 was enacted, and it is in line with Article 117–5 of Regulations 86, promulgated under the 1934 Act. The Bureau, of course, had power to change its ruling, even if the letter be considered as such. *Helvering* v. *Wilshire Oil Co.*, 308 U. S. 90, 100–101. G. C. M. 15438, is not referred to in the opinion below or in Judge Hand's dissenting opinion in the *Pierce* case, though it would have resolved the ambiguity which Judge Hand found in the regulations.

The Treasury Department has, we think, taken the general position ever since 1921, through the predecessors of Article 51–1 of Regulations 86, that even though a joint return is filed only those deductions can be taken which would be allowable to one or the other of the spouses singly. And after the enactment of Section 23 (r) (1) of the 1932 Act gave rise to the specific question here in issue, the only official ruling under that Act unequivocally

interpreted the Act as here urged by the Government.

But whatever the administrative construction of the 1932 Act, the regulations under the 1934 Act admittedly cover the present case, and, we submit, should be controlling. Article 117-5 of Regulations 86, set out *supra,* p. 37, explicitly provides that the limitation "on the allowance of losses of one spouse from sales or exchanges of capital assets is in all cases to be computed without regard to gains and losses of the other spouse upon sales or exchanges of capital assets."

This regulation directly covers the question at bar. The court below gave two reasons for its refusal to give effect to it, namely: (1) that it was invalid because inconsistent, not with the provisions of Section 117 (d), but with the provisions of Section 51 (b); and (2) that the administrative construction had not been consistent and had not in reality received legislative approval. The former contention has been dealt with; the latter, is, we think, untenable.

The asserted lack of consistency in the administrative construction refers to the Commissioner's letter of December 29, 1932. As stated, we do not think that that letter is entitled to any weight, and it was, moreover, tactily repudiated by G. C. M. 15438. In any event some ambiguity in the administrative construction prior to the promulgation of Article 117-5 of Regulations 86 would not vitiate

the effect of subsequent congressional approval of that Article.

The conclusion of the court below that Article 117–5 did not receive legislative sanction is based on the fact that in Section 51 (b) of the Revenue Act of 1938 Congress made certain changes from the 1936 Act in the provisions regarding the filing of joint returns. But Article 117–5 had already received tacit legislative approval when Congress enacted both Section 51 (b) and Section 117 of the Revenue Act of 1936, without change from the 1934 Act. See *Hassett* v. *Welch*, 303 U. S. 303, 312. Moreover, the 1938 modification of Section 51 (b) was directed to a wholly different problem. No change was made in the provision that if a joint return was filed the tax should be computed on the aggregate income, but for the first time the statute provided that liability for the tax should be joint and several. Previous statutes had not contained any provision as to liability for the tax, and two courts had held that in the absence of a provision making the liability both joint and several, one spouse could not be held liable for a deficiency attributable to the other spouse's income. See *Cole* v. *Commissioner*, 81 F. (2d) 485 (C. C. A. 9th), and *Crowe* v. *Commissioner*, 86 F. (2d) 796 (C. C. A. 7th). Accord: *Commissioner* v. *Rabenold*, 108 F. (2d) 639 (C. C. A. 2d), and compare *Rogers* v. *Commissioner*, 111 F. (2d) 987 (C. C. A. 6th). It was solely to remedy this

loophole with respect to the collection of the tax that Section 51 (b) was modified. See H. Rep. No. 1860, 75th Cong., 3d Sess., pp. 29–30; *Commissioner* v. *Rabenold*, 108 F. (2d) 639, 640–641 (C. C. A. 2d); (1940) 49 Yale L. J. 1279, 1284. The enactment of this provision dealing with collection did not in any way indicate Congressional disapproval of Article 117–5 of Regulations 86, which had already received tacit Congressional approval. If Congress had disapproved the interpretation given Section 117 (d) of the 1934 Act by Article 117–5, it would undoubtedly have incorporated in some subsequent act a provision expressly dealing with the treatment of capital losses in joint returns. But it did not do so. While Section 117 of the Revenue Act of 1938 made substantive changes in the treatment of different classes of capital losses, it nevertheless provided that short term capital losses should be deducted only to the extent of short term capital gains, without indicating how the limitation was to be applied in the case of joint returns.

Consequently, the interpretation given the statutory provision by Article 117–5 of Regulations 86, which received legislative approval through the enactment of identical statutory provisions in the Revenue Act of 1936 and of analogous provisions in the Revenue Acts of 1938 and 1939, now has the force and effect of law. *Helvering* v. *Win-*

*mill*, 305 U. S. 79; *McCaughn* v. *Hershey Chocolate Co.*, 283 U. S. 488; *Hassett* v. *Welch*, 303 U. S. 303; *Helvering* v. *Wilshire Oil Co.*, 308 U. S. 90.[11]

## CONCLUSION

For the reasons stated it is respectfully submitted that the decision of the court below should be reversed.

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[11] (1940) 53 Harv. L. Rev. 681, 682, discussing the decision below in the present case, states:

"Thus whatever the merits of the unit theory as a matter of *de novo* interpretation of the policy of a vague statute, it would seem that this was not the construction generally given to it by the courts, or by the Treasury Regulation promulgated under statutory provisions which were subsequently reenacted by Congress."

## APPENDIX

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 23. DEDUCTIONS FROM GROSS INCOME. In computing net income there shall be allowed as deductions:

* * * * *

(j) *Capital Losses.*—Losses from sales or exchanges of capital assets shall be allowed only to the extent provided in section 117 (d).

* * * * *

[U. S. C., Title 26, Sec. 23.]

SEC. 51. INDIVIDUAL RETURNS.

* * * * *

(b) *Husband and Wife.*—If a husband and wife living together have an aggregate net income for the taxable year of $2,500 or over, or an aggregate gross income for such year of $5,000 or over—

(1) Each shall make such a return, or

(2) The income of each shall be included in a single joint return, in which case the tax shall be computed on the aggregate income.

* * * * *

[U. S. C., Title 26, Sec. 51.]

SEC. 117. CAPITAL GAINS AND LOSSES.

(a) *General Rule.*—In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net income:

100 per centum if the capital asset has been held for not more than 1 year;

80 per centum if the capital asset has been held for more than 1 year but not for more than 2 years;

60 per centum if the capital asset has been held for more than 2 years but not for more than 5 years;

40 per centum if the capital asset has been held for more than 5 years but not for more than 10 years;

30 per centum if the capital asset has been held for more than 10 years.

(b) *Definition of Capital Assets.*—For the purposes of this title, "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business.

*       *       *       *       *

(d) *Limitation on Capital Losses.*—Losses from sales or exchanges of capital assets shall be allowed only to the extent of $2,000 plus the gains from such sales or exchanges. If a bank or trust company incorporated under the laws of the United States or of any State or Territory, a substantial part of whose business is the receipt of deposits, sells any bond, debenture, note, or certificate or other evidence of indebtedness issued by any corporation (including one issued by a government or political subdivision thereof), with interest coupons or in registered form, any loss resulting from such sale (except such portion of the loss as does not exceed the amount, if any, by which the adjusted basis of such instrument exceeds the par or

face value thereof) shall not be subject to the foregoing limitation and shall not be included in determining the applicability of such limitation to other losses.

* * * * *

[U. S. C., Title 26, Sec. 101.]

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 51-1. *Individual returns.*—For each taxable year every single person and every married person not living with husband or wife for any part of the taxable year, whose gross income as defined in sections 22 and 116 is $5,000 or over, or whose net income as defined in section 21 is $1,000 or over, must make a return of income. Every married person living with husband or wife for any part of the taxable year, but not at the close of the taxable year, must make a return if his gross income for the taxable year is $5,000 or more, or his net income is equal to, or in excess of, the credit allowed him by section 25 (b) (1) and (3) (computed without regard to his status as the head of a family). (See article 25-7.) A husband and wife living together for the entire year need make no returns unless their aggregate gross income for the taxable year is at least $5,000, or their aggregate net income is at least $2,500. If their aggregate net income for the taxable year is $2,500 or more, or their aggregate gross income is $5,000 or more, either each must make a return, or the income of each must be included in a single joint return. A husband and wife living together at the close of the taxable year but not during the entire taxable year must make a return or returns if their aggregate gross income for the taxable year is $5,000 or

more, or their aggregate net income is equal to, or in excess of, the credit allowed them by section 25 (b) (1) and (3) (computed without regard to the status of either of them as the head of a family). (See article 25–7.) If the income of each is included in a single joint return, the tax is computed on the aggregate income and all deductions and credits to which either is entitled shall be taken from such aggregate income. A joint return of husband and wife may be filed only if they were living together at the close of their taxable year. If one spouse dies prior to the last day of the taxable year, the surviving spouse may not include the income of the deceased spouse in a joint return for such taxable year.

* * * * *

ART. 117–5. *Application of section 117 in the case of husband and wife.*—In the application of section 117, a husband and wife, regardless of whether a joint return or separate returns are made, are considered to be separate taxpayers. Accordingly, the limitation under section 117 (d) on the allowance of losses of one spouse from sales or exchanges of capital assets is in all cases to be computed without regard to gains and losses of the other spouse upon sales or exchanges of capital assests.

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